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Summit Countries: Views on Agricultural Spending*Summary

If the President raises the issue of government support for agriculture during the "unstructured" session at Tokyo, we believe the other leaders would be willing to join the discussion and would likely agree -- at least privately -- that agricultural support programs cost too much. Nonetheless, most would likely refuse to go along with a public statement calling for lower spending on agriculture. Moreover, all the leaders probably would be reluctant to discuss specific measures to reduce spending, fearing such a discussion might become public. The four EC countries and the EC representatives almost certainly would balk at talking about specifics without prior consultation among all the EC countries. In any event, we believe a discussion of particular measures risks breaking down into an acrimonious debate over the various agricultural support programs used by the summit countries. Despite the small size of farm populations in each country, farmers remain a potent political force, and none of the summit leaders appears willing to alienate this voting block. With the exception of Italy, farmers are important supporters of the present ruling parties, and Chancellor Kohl and Prime Minister Nakasone, in particular, are relying on this support in upcoming elections.

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*This paper was prepared by analysts within the Directorate of Intelligence. Questions and comments are welcome and may be addressed to [redacted] Deputy Chief, West European Division, Office of European Analysis, [redacted]

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Japan

We believe Prime Minister Nakasone probably would be willing to discuss, in general terms, ways to reduce agricultural spending, stressing cuts Japan has already made in the last few years. In our view, Nakasone also may agree to a general statement on the need to lower agricultural support, but Tokyo's actual latitude in implementing spending cuts is extremely limited. If the discussion becomes heated, Nakasone will probably limit his comments, preferring to let the United States argue with EC countries. []

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Nakasone almost certainly would not agree to calls for major cuts in Japanese agricultural support. The ruling Liberal Democratic Party depends heavily on financial and electoral support from farm interests and is unlikely to risk alienating farmers, particularly if Nakasone and the party call general elections in June. There still is a strong consensus favoring protection for Japanese farmers in the ruling Liberal Democratic Party (LDP) because two-thirds of LDP Diet members have rural or semi-rural constituencies. In addition, opposition parties are more likely to attempt to woo farmers from the LDP than to run on an anti-farm spending platform. In fact, the Japan Socialist Party, the largest opposition party, depends on rural support for over half its Diet seats. []

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In any discussion of agriculture, Nakasone is certain to point out that Japan has reduced agricultural spending by about 10 percent over the past two years as part of an overall austerity program. The focus of agricultural spending also has changed. Direct commodity subsidies have been reduced by about 25 percent since 1983, shifting the focus of the government's program toward infrastructure projects and research. Further cuts probably would go beyond politically acceptable levels. []

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We believe, however, that Nakasone may take some steps in the next few months on agricultural liberalization aimed at the United States. To ease trade friction with the United States and avoid GATT or Section 301 action, Tokyo is considering loosening import quotas on 12 farm items -- including processed meats and fruits -- by the end of April. Even if Tokyo only partially accedes to US demands for easier access to Japanese agricultural markets -- as now appears likely -- there will be some backlash among Japanese farmers. In our opinion, the consequences would further reduce Nakasone's latitude to implement other

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agricultural spending cuts this year because Tokyo will have either liberalized agricultural imports or suffered punitive trade measures from the United States -- and either alternative would harm farmers. [REDACTED]

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West Germany

Chancellor Kohl probably would agree that West Germany is spending too much on the agricultural sector, but he is unlikely to be willing to discuss specific measures to curb such support. The Kohl government, like its predecessors, has on numerous occasions called for new efforts to rein in EC agricultural spending to curb the growing drain on government revenues -- West Germany is the largest contributor to the EC budget. Despite such calls, the Chancellor almost certainly will not agree to publicly support agricultural reform initiatives at Tokyo because the farm vote will be vitally important to the coalition's prospects in the January 1987 election. The farm vote is the stronghold of the Christian Democratic Union/Christian Social Union (CDU/CSU), but it is relatively unimportant for the Social Democrats and Free Democrats (FDP). Typically, 80 to 90 percent of farmers vote CDU/CSU. [REDACTED]

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Moreover, the CDU/CSU is worried that losses in recent state and municipal elections were partially due to declining support from the rural population, mostly by farmers abstaining from voting, according to US Embassy reporting. The CDU/CSU-FDP government has been subject to harsh criticism in rural areas as a result of declining farm income, difficulties with the introduction of a new EC milk quota system, and somewhat lower grain prices. [REDACTED]

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Therefore, the CDU/CSU is attempting to polish its image prior to pending state elections and the January federal election by announcing increased support for agriculture. A joint committee led by Lower Saxony Minister President Ernst Albrecht has just published a new CDU/CSU agricultural policy platform. The document, largely a collection of previous proposals, clearly is designed to impress the rural population. It shows that the coalition has no intention of tackling the skyrocketing costs of agricultural support in this election year. On the contrary, it will be even more generous in an attempt to cushion rural unrest. [REDACTED]

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Although Bonn has acknowledged the need to curb EC agricultural production and spending, over the past two years it

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has battled the EC to protect West German farmers from changes in the Common Agricultural Policy (CAP). In 1984, the EC began eliminating positive monetary compensatory amounts (MCAs), which have had the effect of subsidizing West German agricultural exports to other EC countries. To ease the burden of this change on West German farmers, Bonn fought for and won authorization to add 5 percentage points to its 8-percent domestic value-added tax on agricultural products. The extra revenue will be used to compensate farmers for the loss of funds derived from MCAs, and, in effect, creates a new national aid to agriculture. Government contributions to farmer pensions also were raised and more cash pumped into poorer rural areas. Last June, Agriculture Minister Ignaz Kiechle invoked West Germany's first-ever EC veto to block a proposed cut in the price supports paid to cereal growers. Bonn is equally determined this year not to allow CAP reforms in the grain sector to lower farmers' incomes.

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In addition to the CAP, West Germany supports agriculture through national programs, which include farm consolidation, gasohol promotion, interest subsidies for farm investment, and measures benefiting individual farms -- mainly various types of investment aid. The objective of farm consolidation is to increase efficiency by reducing the excessive number of individual plots. It does so principally by providing low-interest loans to farmers to acquire additional land. Gasohol is the major product of extensive research support to improve the methodology for turning plant material into industrial products to offset surplus production. Federal expenditure for direct agricultural support programs officially totaled \$620 million in 1984, with state programs probably adding another \$200 million or so. A respected West German economic research institute estimated that in 1984 agriculture was West Germany's most highly subsidized economic sector, with subsidies -- excluding those from the EC -- of over \$3,000 per employee versus an industry average of about \$450.

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France

The French are likely to be both guarded and suspicious in their reaction to a US-initiated discussion of reductions in agricultural spending. Although President Mitterrand may be willing to discuss the problem of agricultural overspending privately and informally at Tokyo, he will almost certainly oppose any move by the summit countries to address the issue formally and concretely. Moreover, the domestic political maneuvering now going on in France suggests that French officials

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will be quick to disavow publicly any reports that hint at an agreement to reduce government spending on agriculture. [redacted]

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The novel experiment in powersharing between a Socialist president and a conservative prime minister could lead both officials to be more protective of French farmers than they might otherwise be. Mitterrand will be accompanied at Tokyo by Prime Minister Chirac, who made the plight of French farmers an important theme in his election campaign. Chirac attacked the agricultural policy of the Socialists, charging that it had sacrificed French farm interests by accepting reform of the EC's CAP. One of Chirac's campaign promises was to raise farm incomes, through increased EC export subsidies if necessary. Chirac has apparently decided to stick to this tough agricultural policy line now that he is in office; he has selected Francois Guillaume, head of the largest farmers' union and one of the most militant champions of French farmers, as Minister of Agriculture.

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Chirac's views on agricultural policy will certainly color Mitterrand's response to any discussion of lowered subsidies. Mitterrand -- who is also a staunch defender of French agricultural interests -- would not want to leave himself open to charges that he sold out French interests, especially in the face of US pressure. Any such appearance of weakness would play into the hands of Chirac, who is trying to build domestic political support for a Presidential bid in 1988. For his part, Mitterrand also is looking for issues that will boost him domestically, and standing up for French farmers has traditionally been popular in France. Thus, in our view, the jockeying between Mitterrand and Chirac makes it even more likely that both will hang tough in agricultural policy discussions at Tokyo.

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French officials will, moreover, be suspicious of any US efforts to raise the contentious agricultural trade issue. In discussions with US diplomats, French officials have criticized what they see as new aggressiveness in US trade policy, which they feel is too frequently aimed at France. Mitterrand will be very sensitive to the possibility of being caught unaware or "ambushed" by the United States--as he thought he was at the Bonn Summit last year. In addition, Mitterrand wants to avoid a situation where he feels that EC solidarity is being threatened. He may argue, therefore, that EC members must settle the issue of CAP reform among themselves and arrive at a common position before talking with third countries. He may also contend that the GATT, and not the Summit, is the appropriate forum for addressing agricultural spending reform.

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All this is not to say that Mitterrand is insensitive to the problem of agricultural overspending. France became a net EC contributor for the first time last year, and most working level officials in Paris recognize the need to curb runaway CAP spending. Given the domestic political pressures they face from the most militant and well-organized farmers in the EC, however, French officials are convinced that agricultural reform must be undertaken gradually. We believe that France also will avoid exposing itself to outside pressures while trying to accomplish this difficult task. Thus, in our view, despite any private acknowledgements that agricultural overspending is a problem, Paris will remain loath to put anything specific on the table.

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United Kingdom

We believe that Thatcher probably would be willing to join a general discussion of reducing government spending on agriculture and promoting freer agricultural trade, but she would likely balk at consideration of specific measures. In our opinion, Thatcher almost certainly would like to cut subsidies but would prefer to see the United States take the lead in pushing any reform proposals. She would likely refuse to commit herself to specifics before testing domestic sentiment and reaching an EC consensus, partly to avoid more criticism that she too often aligns Britain with the United States rather than her EC partners.

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In our opinion, Thatcher probably would point to steps London is already taking to deal with agricultural spending. She has strongly urged reform of the CAP -- to which Britain is a net contributor -- but is concerned that increased agricultural support by other countries, particularly the United States, may undermine any EC reform efforts. British officials have told their US counterparts they will resist any CAP reform that penalizes efficient British farmers rather than inefficient European farmers. The United Kingdom also has expressed support for including agriculture in the new GATT round and believes that this is the appropriate forum for broad discussion of agricultural trade issues.

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British farmers -- through the National Farmers' Union (NFU) -- are one of the country's most politically pragmatic and influential lobbies. Farm lobbies traditionally have been one of the strongest bastions of Tory support; such contemporary Tory luminaries as Lord Whitelaw, Francis Pym, Peter Walker, and Michael Heseltine are either farmers or large landowners.

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Although Prime Minister Thatcher's 11-year tenure as party leader has begun to give the Tories a more urban and commercial cast, political support in rural England remains a key to the Conservatives' electoral prospects. [REDACTED]

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Both Labor and Conservative governments have actively supported agricultural interests by adopting legislation designed to stimulate domestic production and limit foreign competition. As a result of these policies, by the 1980s Britain produced more than 70 percent of the foodstuffs it consumed -- compared to only 30 percent before World War II and 50 percent at the end of the 1960s. When Britain joined the EC in 1973, the domestic subsidies already enjoyed by British farmers were enhanced by the additional protection afforded by high EC tariffs. [REDACTED]

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As a result of government subsidies and EC programs, farmers largely escaped the 1979-82 recession. Since Thatcher's 1983 reelection, however, the agricultural climate -- as well as farmer support for Thatcher -- has changed for the worse. Farm income in 1985 was 43 percent lower than 1984, largely because of unfavorable weather conditions. In addition, EC quotas on milk production to reduce the surplus have lowered the income of British milk producers for the past several years. Farm lobbyists claim efforts to reduce the cereals surplus will also disproportionately burden British farmers. In addition, Thatcher's effort to hold down both domestic and EC spending has brought charges from the NFU that the Prime Minister is partly responsible for the damage to farmers. [REDACTED]

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Italy

We believe Italian Prime Minister Craxi probably would go along with a discussion of government spending on agriculture, but he would not be a very active participant in the talks. Moreover, he is likely to discourage a lengthy discussion of the subject at Tokyo and would avoid specifics. Craxi generally has limited interest in agricultural issues because he gets little political support from the farm sector and only a small portion of Rome's budget -- about 1.5 percent -- goes directly to farm programs. In our opinion, he may fear that a detailed discussion would [REDACTED] undermine the image he wishes to project of a serious, well-informed world leader. If the discussion threatened to become too detailed, Craxi probably would argue that the Summit is not the best forum for the issue; that agriculture is a topic for the new GATT round; and that, at the very least, the EC must reach internal agreement before participating in a broader international discussion. [REDACTED]

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Although the Italian agricultural sector's share of total employment (12 percent) remains high in relation to other European countries, Italian farmers wield less political power than their European counterparts. The small size of the family farm, divergence of policy interests arising from the diversity of goods produced, differing political affiliations of the major agricultural organizations, and the immense political power held by Italy's industrial families all tend to undermine the agricultural sector's political influence. Italian farmers tend to support either the Christian Democrats or the Communists, but no major Italian politician champions agricultural issues or relies heavily on farmer support. Consequently farming has, by and large, been slighted in national spending programs. [redacted]

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A few national programs have been implemented, but most have been poorly administered and ineffective. A ten-year agriculture development plan approved in 1977 allocated \$8 billion for mechanizing farms, improving rural infrastructure -- particularly in the south -- and increasing marketing services. The government also provides subsidized credit to farmers. [redacted]

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Italian agricultural interests are more often than not at odds with EC agricultural policy. Italy's major farm exports -- citrus, olive oil, and wine -- compete for EC markets with North African produce that enjoys preferential access. On the other hand, the goods Italy imports from its EC partners -- meat, dairy products, and cereals -- are highly priced, and Italian production of these goods is discouraged by EC programs aimed at reducing surplus production -- most of which is generated by northern EC countries. Italy's agricultural trade deficit -- about \$5.7 billion in 1985 -- is second only to fuel as a contributor to Italy's overall trade imbalance. Last November, Craxi launched an investigation into means to reduce Italy's food deficit; the final report will undoubtedly include criticism of the EC agricultural policy. Like other EC countries, however, Italy relies heavily on EC programs to support its farmers and Rome supports the idea of an EC-wide agricultural policy despite problems with some of its programs. Italy is a net benefactor from the CAP -- it receives more money from the EC than it pays in -- and we believe Craxi would argue that any problems Italy has with the CAP must be worked out within the EC rather than at the Tokyo Summit. [redacted]

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Canada

We believe Prime Minister Mulroney almost certainly would be willing to discuss the idea of reducing government spending on agriculture and freeing international agricultural markets, but he probably would refuse to discuss specifics or make definite commitments. During his 1984 election campaign and in subsequent statements, Mulroney expressed support for the general principle of reducing public spending and removing government subsidies in order to promote competition. Nonetheless, Mulroney is under heavy pressure to maintain support for farm interests. The core of Tory political support is located in Canada's western agricultural provinces: the party now holds 79 of 81 parliamentary seats there. Moreover, Prime Minister Mulroney is unlikely to support major cuts in agricultural subsidies for reasons of national psychology. Like Americans, Canadians have a deeply rooted, sentimental attachment to the "family farm" that cuts across economic class and party line. Unlike in the United States, however, there is virtually no opposition to the substantial financial aid now given to agriculture. The political importance of farmers is so strong that the Tories appear ready to boost federal export subsidies for grain to whatever extent is necessary to protect Canada's share of the world market. [REDACTED]

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Ottawa's spending on agriculture goes far beyond the \$1.25 billion listed in its budget for fiscal 1986-87. Canadian governments, for example, have long subsidized the transportation of grain by rail: between 1867 and 1984 grain farmers paid a constant freight rate of only 1/2 cents per ton/mile. In recent years, Ottawa has spent large sums on building grain ports at Prince Rupert, British Columbia, Churchill, Manitoba, and Thunder Bay, Ontario. Most recently, Mulroney reaffirmed his Liberal predecessor's pledge to substantially upgrade the government-owned railway from Winnipeg to the Pacific to speed the movement of grain. Finally, large sums have been invested in the St. Lawrence Seaway and its canal system to enhance grain-exporting capabilities and develop an Atlantic grain port at Sept-Isles, Quebec. [REDACTED]

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Federal subsidies for agriculture also are included in budget provisions dealing with taxation and social policy. Ottawa, for example, frequently exempts farmers and fishermen from paying the federal sales tax on fuel. Both are also often given lower qualifying requirements for unemployment insurance if a year's harvest or catch is poor. Ottawa administers price stabilization

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plans providing advance payments to farmers for spring seeding and to fishermen for the repair or purchase of boats and gear. Ottawa also runs marketing and sales services to facilitate the export of grain, fish, and dairy products. Finally, much federal agricultural aid is mirrored by similar programs in most of Canada's 10 provinces. []

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European Community

We believe EC officials probably would be willing to discuss informally the need for curbing agricultural spending, but they will not be able to make any specific commitments without the approval of all the member states. Both Dutch Prime Minister Lubbers -- attending the Summit as the current President of the EC Council of Ministers -- and EC Commission President Delors are committed to cutting the cost of the EC's CAP and solving the problem of surplus production. They must, however, work within the constraints imposed by political considerations within the member states. []

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Though Delors and Lubbers appreciate the importance of reducing agricultural spending, we believe they may point to establishing order in world agricultural markets as the most significant immediate agricultural problem that could be discussed informally at the Summit. The Commission is concerned that the US export enhancement program will cut into the EC market share. The Community has aggressively defended and expanded its market share in the past, and can be expected to compete with the US program. The Commission finds market sharing arrangements between the major exporters to be appealing, and Delors could raise the idea as a way to avoid an export subsidies war. In our opinion, the EC representatives undoubtedly would oppose proposals to create a totally free market for agricultural goods -- an effort that would eliminate the CAP, the EC's most important community-wide program. []

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The EC, in the face of growing agricultural surpluses and an impending budget crisis, already is struggling with the problem of cutting agricultural spending. There is a growing realization among agriculture officials at the Commission and in the member states that the cost of the CAP -- totaling \$20 billion for 1986 and accounting for 67 percent of the entire EC budget -- is wasteful and diverts resources from other important endeavors such as research and development. Although the CAP has vastly exceeded one of its original goals -- to provide food self-sufficiency -- and is driving the budget into the red, no plans are in the making to fundamentally overhaul the system. []

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The EC Commission probably is the leading proponent of reforms to control CAP spending and curb overproduction. In July, Agriculture Commissioner Andriessen unveiled a "green paper" calling for a more market-oriented approach to setting EC farm prices. He has proposed a general price freeze for the 1986-87 marketing year, with price cuts for the grain sector, a 3-percent tax on production to finance export subsidies, higher quality standards, and a shortening of the period during which the EC will buy a farmer's crop. Measures to cut beef and milk production also were proposed. [REDACTED]

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In the past, however, the member states have watered down Commission efforts to control spending and production, and are currently deadlocked over the 1986-87 proposals. There is a general consensus among the agriculture ministers that a price freeze is unavoidable because of an impending budget crisis. This year, because of the fall in the dollar and the resulting need for larger export refunds to cover the widening gap between world agricultural prices and internal EC prices, the EC is facing an estimated \$3 billion deficit that will have to be covered by special member state contributions. Nevertheless, there is marked disagreement on the other Commission proposals. In our opinion, the need to achieve unanimous agreement ensures slow decisionmaking and a solution representing the lowest common denominator. Though eventually the members will probably agree to some reduction in CAP spending, they are highly unlikely to alter a fundamental feature of the system behind the overproduction -- the commitment, based on national politics, to guarantee farm incomes. [REDACTED]

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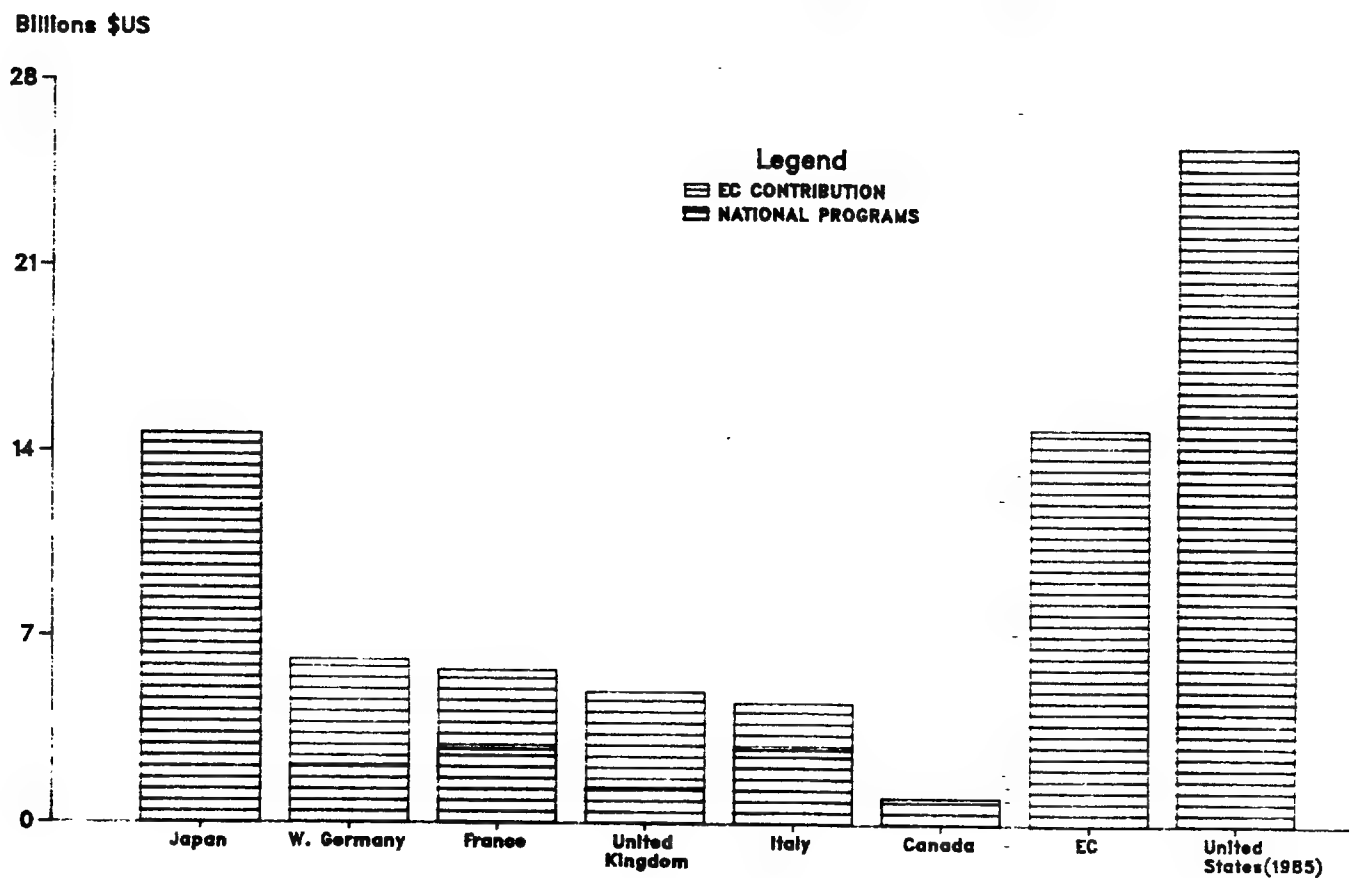
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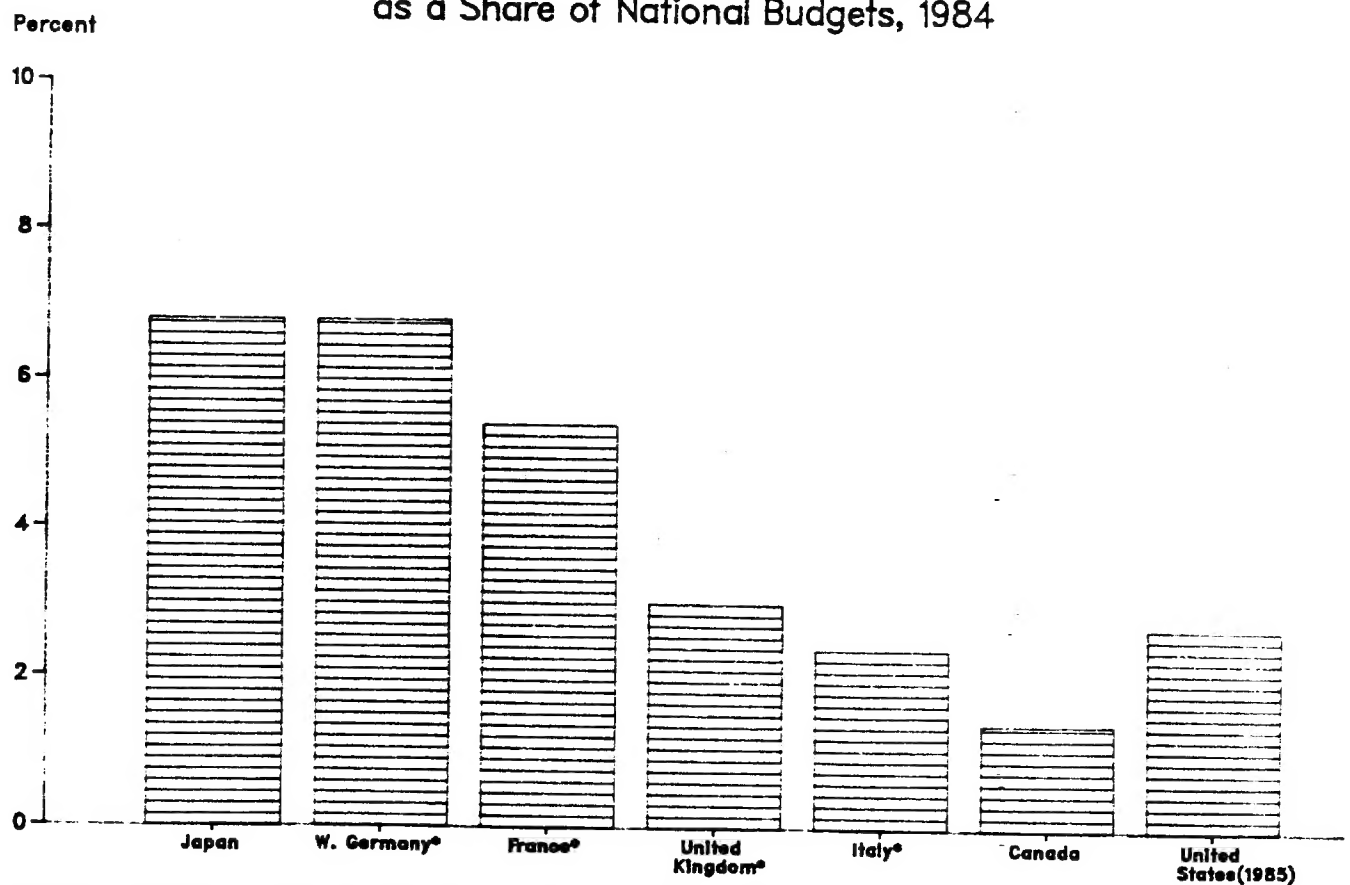
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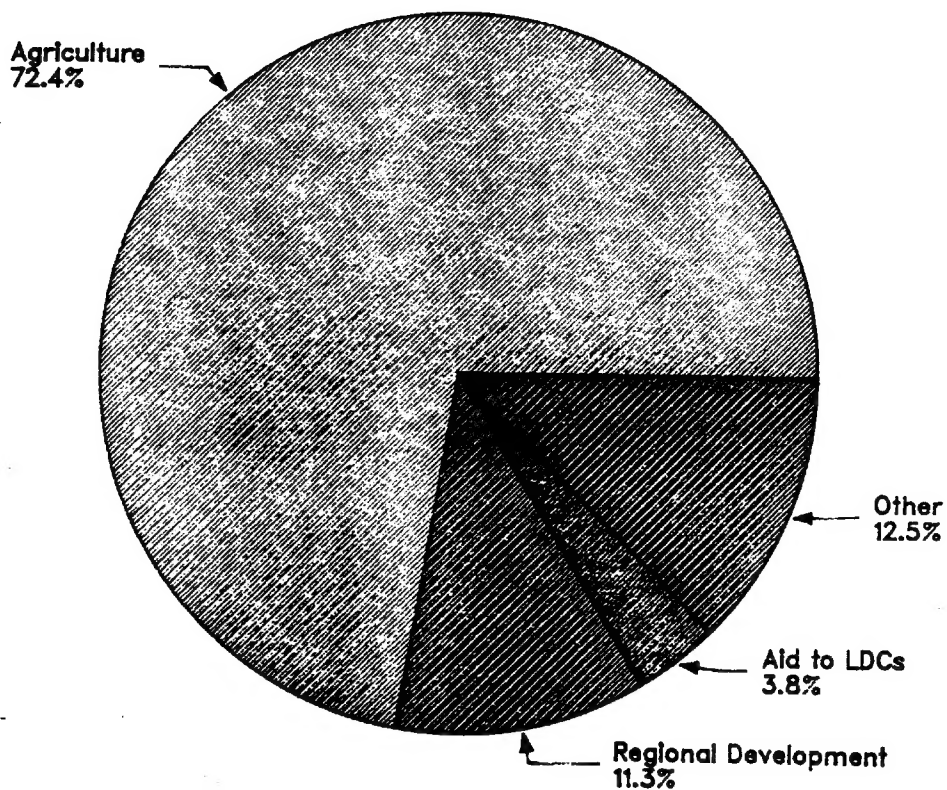
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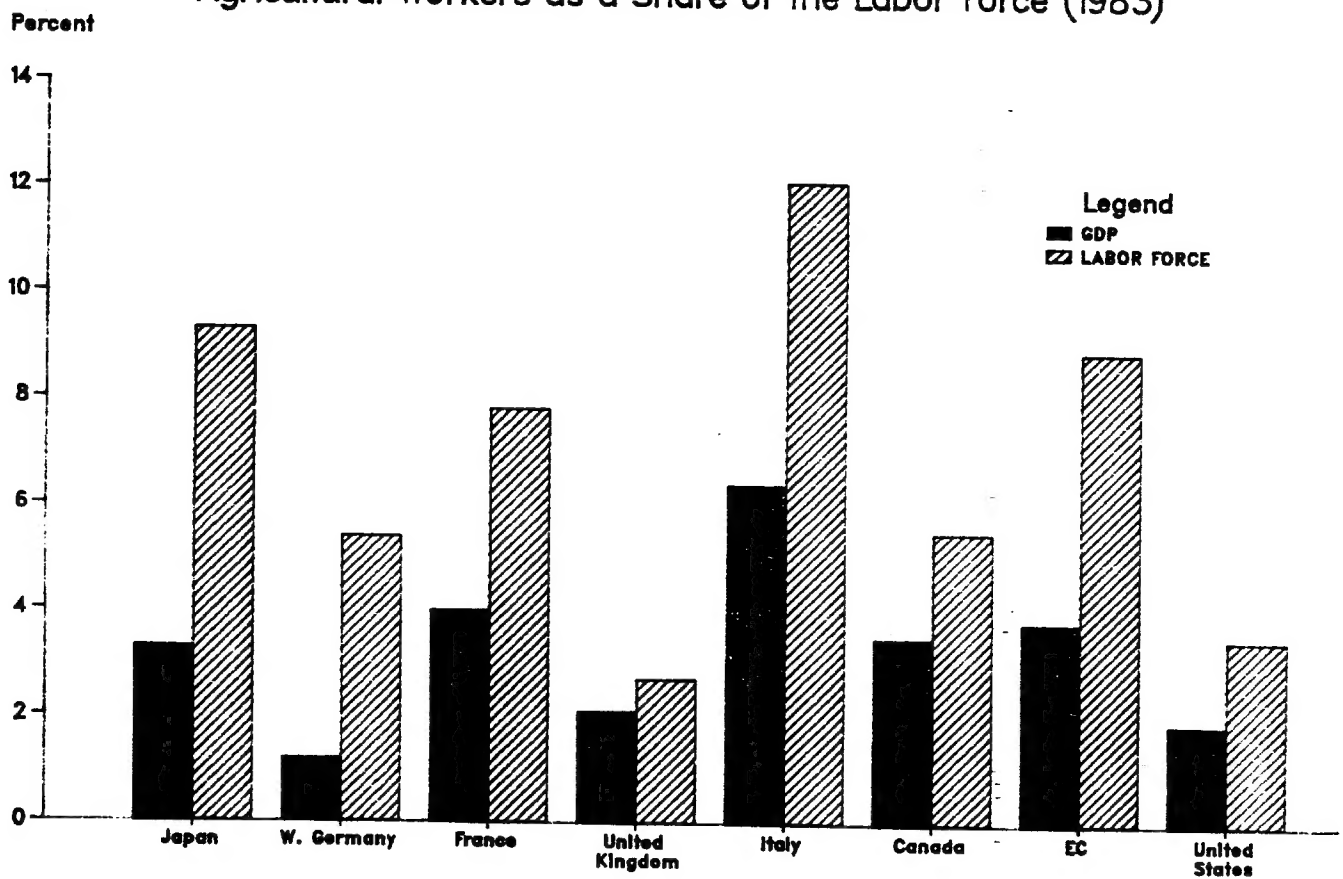
**European Community:
Distribution of Budget Expenditures, 1984**

(\$20.6 Billion)



SUMMIT COUNTRIES:

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